Engagement and Voting examples

Engagement

Given the impact of Covid-19, company engagement took on even greater importance during 2020. Aberforth sought to understand how companies were dealing with the operational and financial implications of lockdown. This was especially important in light of the relaxation of pre-emption guidance, which allowed companies to issue up to 20% new equity without pre-emption rights. Engagement enabled better understanding of restructuring or capital allocation changes resulting from Covid-19 and of how investee companies were likely to emerge as restrictions were lifted.

During 2020, Aberforth engaged with the executives of every investee company, both after results and on an *ad hoc* basis in between. There were also numerous engagements with non-investee companies as part of the usual investment due diligence process. In 2020, Aberforth conducted 396 formal meetings with executives, a number that excludes *ad hoc* interactions by phone or email. In addition to these meetings, Aberforth conducted 125 engagements with the chairs or non-executives of 60 investee companies. Beyond routine corporate governance matters, some of these meetings addressed relatively complicated issues that required multiple engagements. In some cases, these engagements are on-going.

Set out below are a number of examples that illustrate the breadth and depth of engagements carried out during 2020.

Example: The Restaurant Group

Aberforth continued its engagement after voting against the acquisition of Wagamama in 2018, and the re-election of the chair and SID in the subsequent AGM. As a leisure business with physical venues, The Restaurant Group has been adversely affected by Covid-19, but executive management have performed well to reposition the business as demand recovers. However, lockdown has challenged the balance sheet and refinancing is probable. Aberforth's confidence in the chair's oversight of capital allocation was shaken by the heavily dilutive Wagamama acquisition, which continues to affect the company's stockmarket valuation. Accordingly, Aberforth believes that it is in the interests of all shareholders for a new chair to be appointed and again voted against the re-election of the chair.

Example: SIG

SIG's chairman acted decisively to address poor historical performance, articulating a cogent and refreshed strategy. However, the impact of the pandemic made additional capital funding inevitable. A depressed stockmarket valuation, together with confidence in SIG's market leading position and the ability to generate higher returns over time, gave confidence in significant upside and encouraged us to support strengthening the capital structure for the long term. Engaging proactively with the chair, Aberforth provided indicative support ahead of a £165m equity capital raise, which completed on 9 July 2020. The structure of the equity raise was a firm placing and placing and open offer, which afforded greater flexibility in allocating new shares but came with the risk of dilution to existing shareholders. Usually, Aberforth's proactive engagement and support mean that clients' stakes can rise through the firm placing. However, in the case of SIG, this did not apply. Amid its refinancing discussions, the board was approached by Clayton Dubilier & Rice (CDR). The outcome of negotiations was that CDR would invest £82.5m through the equity issue to take a 26.7% stake and two board seats. Aberforth was consulted and judged that, in view of the circumstances and despite ownership dilution, it represented the best outcome for clients' capital. "PIPE" deals such as this are relatively uncommon in the UK, though better established in the US.

Example: Company A

Aberforth's clients are one of the largest shareholders in company A. In the years before the pandemic, the company had rebuilt its reputation and strengthened its balance sheet following previous over-expansion. The onset of Covid-19 threatened to undo this rehabilitation and the board proposed raising additional equity, as well as cutting the dividend, to protect the business.

To ascertain the need for additional equity, Aberforth had numerous meetings with the executive team and chair to understand the assumptions behind their downside scenario analysis. Having assessed this, and taking into account industry dynamics, Aberforth argued that there was not a need for equity at that time. The company did not raise new capital. This was a difficult decision given the significant prevailing uncertainty, but it proved correct given the subsequent return to profitability, resumption of dividends and avoidance of dilution.

Example: Gulf Marine Services

Following proactive involvement with the board in the appointment of the chair, Aberforth worked closely with the chair in respect of a restructuring proposal, which would have involved an equity raise and the deleveraging of the operating business. During this process the company was subject to a bid by a competitor, Seafox International, at a level that failed to reflect the long-term value of the business. The bid was unsuccessful but, through a series of Extraordinary General Meetings, Seafox was subsequently able to remove existing directors and appoint its nominated individuals as directors. Aberforth voted against all such proposals and separately contacted the Takeover Panel to express concern about the process and ability for Seafox to gain effective control of the business despite their previous failed bid attempt.

Example: Lookers

A potential fraud and weaknesses in accounting process caused a delay to the publication of its financial statements and the temporary suspension of the shares from 1 July 2020. Against this background, Aberforth increased engagement with the company, focusing on (a) the reasons for the publication delay, (b) the necessary steps required to strengthen governance, (c) the composition of the board and (d) remuneration, specifically, malus and clawback provisions. The chair and senior independent director reassured that the board was alert to these concerns and would take the necessary steps to enhance governance, systems, and controls. Subsequently, the search for a new chair commenced and, in this regard, engagement continues.

Example: Non-Standard Finance

Investment in this branch based non-prime lender was made for the prospect of organic growth through increasing the number of branches, with the expansion risk mitigated by robust underwriting from the face-to-face pre-lending process. Aberforth cautioned against the launch of a bid for Provident Financial questioning the timing and suitability of such an approach. This advice went unheeded, which led to extensive engagement with the chair and other non-executive directors to determine the level of scrutiny over the executives. Failing to reach a satisfactory conclusion, Aberforth lost confidence in the chair, informed him and voted against his re-election at the AGM. As these concerns continued to be overlooked, it was decided to sell clients' holdings in the company.

Example: Kenmare Resources

During 2020, Kenmare Resources successfully completed the movement of a dredge and 7,100 tonne wet concentrator plant 23km to a new, higher grade, mining area. The project should transform Kenmare's production and profit growth prospects for the medium term and should result in significant cash generation once fully operational. Aberforth conducted several engagements with the executive team and chair about capital allocation, expressing the view that, in light of limited future capex requirements, a significant proportion of the cash generated from the expansion should be returned to shareholders through cash dividends.

Health and safety is a crucial focus for mining companies, including Kenmare, with potentially significant negative repercussions for poor operating standards. The company has a good record, so it was sad and surprising when a casualty was reported at the Moma mine in 2020. Aberforth engaged with Kenmare to understand the circumstances behind the fatality. It was explained that the death was not related to mining activity and that there had been no lapse in operating standards.

Example: Air Partner

Clients of Aberforth had been longstanding investors in this aviation services business and one of the largest shareholders. Initially, Air Partner was a beneficiary of Covid-19 as the company was at the forefront of repatriating citizens and moving PPE across the globe. Naturally, this extra demand filtered into a stronger profit outlook, improved balance sheet position and a much higher share price. Despite this, the board approached major shareholders with a view to issuing equity to strengthen the balance sheet further.

Aberforth conducted several meetings with the executive team and chair to understand the assumptions behind their analysis. Having assessed this, Aberforth decided there was not a need for equity at that time and relayed this message to the chair. Unfortunately, this engagement proved ineffectual and the company proceeded with the equity raise. This led to the sale of clients' holdings in the company.

Collective engagement

Working with other shareholders can be an important option in Aberforth's approach to stewardship with its investee companies. In 2020, there were six examples of collective engagement involving dialogue with other institutional investors. Several of these engagements continue into 2021. While all of these instances remain sensitive in nature and disclosure at this time would be counterproductive to the engagement objectives, it is the intention to disclose in due course when matters are concluded.

Voting

Voting principles

Aberforth:

- Votes to maximise the value of its clients' capital, taking into account all relevant factors, including environmental and social issues.
- Votes on all resolutions put to shareholders.
- Does not automatically follow the recommendations of the board, or of proxy advisers, but aims to engage with the board before voting against or abstaining.
- Believes that abstention – or withheld votes – can be a useful signal in on-going engagement with a company.
- Expects to be consulted on contentious issues before they are brought forward for voting.
- Expects companies to comply with the Corporate Governance Code 2018 or explain otherwise.
- Retains a flexible and pragmatic approach recognising that the requirements of smaller companies do not always conform with "one-size-fits-all" policies.

Below is a breakdown of how Aberforth voted during 2020, which is followed by several examples that provide more detail on the rationale behind certain voting decisions.

Voting	12 months to 31 December 2020
Shareholder meetings at which our clients' shares were voted	108
Shareholder meetings at which our clients' shares were voted against or abstained (1)	25
Number of resolutions voted	1,669
Number of resolutions voted against	33
Number of resolutions abstained	21

Notes:
(1) On one or more resolutions

Non-Standard Finance

Voted AGAINST re-election of the chairman

Following the extensive engagement described earlier in this report, Aberforth lost confidence in the chair and voted against his re-election at the AGM.

The Restaurant Group – consolidated into single example below

Voted AGAINST re-election of the chairman

TI Fluid Systems

Voted AGAINST remuneration

As was the case in previous years, the potential rewards from the variable element of the proposed remuneration package were excessive – these could see the executives earn seven times their salary.

Amigo Holdings

Voted AGAINST board changes – several occasions

Two general meetings were requisitioned by the majority shareholder, Richmond Group. On both occasions, Aberforth voted against the proposals to remove the board of directors in favour of Richmond Group representatives. This would not have conformed to governance standards and potentially left the company at risk of not complying with certain FCA regulatory requirements.

Gulf Marine Services

Voted AGAINST shareholder proposal to change the board

As discussed in the Engagement examples, Seafox were unsuccessful with a bid for the company, but, through a series of Extraordinary General Meetings, was ultimately successful in appointing its nominated directors to the board, effectively achieving control of the company. Aberforth voted against all such proposals and contacted the Takeover Panel to express concern about the process and ability for Seafox to gain effective control of the business despite their previous failed bid attempt.

SDL

Voted AGAINST scheme of arrangement – proxy advisor was FOR

Voted AGAINST merger agreement – proxy advisor was FOR

Aberforth voted against the Scheme of Arrangement for the takeover of SDL by RWS. This was motivated by the all-paper terms of the deal, which exposed the clients to a richly valued company that, by virtue of its AIM listing and large size, could not be a long-term holding.

Whilst voting FOR a resolution does not usually merit explanation, there are circumstances in which such votes are significant. The example below covers one occasion and demonstrates the importance of combining voting decisions with engagement.

Lookers

Voted FOR re-election of chair and non-execs

Following the company's potential fraud and delay to the publication of financial statements, Aberforth initially intended either to abstain or vote against a suite of non-executive directors, including the chair. In line with usual practice when considering such votes, Aberforth engaged with the company to explain the rationale. As part of that engagement process, the board offered reassurance that it was aware of the issues and that governance was not at odds with shareholders' interests. The discussion centred on the importance of not destabilising the board while it finalised the publication of the delayed financial statements. Pragmatically, therefore, the initial intention was reversed and votes in favour of the re-election of the chair and non-executives were lodged.

Votes different from proxy advisor recommendation

During 2020 there were 65 instances, in which Aberforth did not follow the voting recommendations of its proxy adviser. Some examples are set out below.

The Restaurant Group

Voted FOR remuneration policy – Proxy advisor was AGAINST

Voted FOR restricted share scheme – Proxy advisor was AGAINST

Voted AGAINST chair – Proxy advisor was FOR

Aberforth has engaged extensively with The Restaurant Group since investing in 2016 and continued to do so in 2020. The expensive and dilutive acquisition of Wagamama in 2018 raised concerns about the company's governance, which culminated in a vote against the transaction. During this process, engagement with the chair, and SID at the time, was unsatisfactory, which led to votes against at subsequent AGMs.

The pandemic exposed the misallocation of capital, with the business carrying too much debt and facing a significant loss of earnings. Aberforth supported a necessary equity issue: concerns about the chair were outweighed by confidence in the new CEO, who used the crisis to aggressively re-position the business away from underperforming legacy sites through a CVA. This significantly reduced the lease exposure of the company and improved future profit potential.

Despite these efforts, the executives did not have suitable incentives in place, with cash bonuses cancelled to conserve cash and LTIPs significantly under water. Further engagement with the board gave comfort about a proposed restricted shares scheme with profit underpin. Accordingly, Aberforth voted in favour of remuneration changes, which was against the recommendation of the proxy adviser.

Redde Northgate

Voted FOR remuneration policy – Proxy advisor was AGAINST

The proxy adviser judged that a vote against the remuneration policy was warranted since concerns persisted about the Value Creation Plan. Aberforth engaged with the chair before the vote to understand the nature of the arrangements. The company confirmed that it would consult with shareholders, review the on-going appropriateness of the scheme and that no awards would be made under the plan in 2020. In light of this, a vote in favour was justified. As regards the remuneration report, the proxy adviser also recommended a vote against. In order to ensure alignment with shareholders, Aberforth agreed with the chair that there should be an incentive award, which recognised the aims of the newly enlarged group and the skills and experience of the executive directors. A vote in favour of the remuneration report was therefore warranted.

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